

COVID-19: AN INTERNATIONAL CONSTRUCTION PERSPECTIVE – GERMANY

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THIS IS THE SECOND OF OUR FIVE-PART SERIES COVERING THE ISSUES FACING THE CONSTRUCTION INDUSTRY IN FIVE DIFFERENT JURISDICTIONS ACROSS THE WORLD IN THE FACE OF THE COVID-19 PANDEMIC.

Jurisdictional considerations

There is no one standard form construction contract used in the German construction sector. However, many contracts, particularly those involving public authorities, use the terms and conditions set out in the “VOB/B”.¹ In addition, since 2018, the German Civil Code has set out default provisions for construction contracts which parties can choose to incorporate into their agreements, and which will apply if no explicit choice has been made. Finally, larger international projects, as well as plant construction contracts, often use FIDIC standard form contracts.

"In Germany, commercial parties often prefer to refer disputes to arbitration pursuant to the rules of one of the national arbitral organisations."

Save in relation to FIDIC contracts, German construction contracts do not typically include comprehensive provisions regarding force majeure, corresponding risk of increased costs, time delays or compensation and termination. As a result, it is necessary to consider the general principles of German civil law.

Although parties to German law governed construction contracts are largely free to agree appropriate dispute resolution provisions, the public sector generally prefers disputes to be referred to the courts. By comparison, commercial parties often prefer to refer disputes to arbitration pursuant to the rules of one of the national arbitral organisations. In addition, several forms of adjudication procedure are available to assist in the determination of disputes.

Generally speaking, German courts are very reluctant to release a contractor from their contractual obligations, and in order to bring a successful claim for additional costs incurred as a result of a force majeure event, it is necessary to satisfy a high burden of proof. However, German law normally grants relief from liability for delay or other damage resulting from a force majeure event, provided reasonable preventive measures have been taken against foreseeable consequences.

Force majeure and frustration

There is no legal definition of force majeure under German law, but German jurisprudence has developed a definition which is close to that found in international construction contracts. In brief, a force majeure event can be defined as being an external event which cannot be foreseen even by applying the greatest possible care (thus being unforeseeable) and cannot be prevented by applying all reasonable measures (thus being unavoidable). It is likely that the COVID-19 pandemic will qualify as a force majeure event under German law. However, that does not necessarily mean that specific legal or contractual consequences will result. Instead, under German law it will be necessary to consider the specific effects of the pandemic on contractual performance.

Under the German Civil Code, a force majeure event usually entitles a contractor to an extension of time for completion of the works, provided that the contractor is not responsible for the delay. However, it is usually not possible to claim for additional costs. It is only in exceptional circumstances, where continuation of the contract would cause “unbearable hardship” to the contractor, that they may be able to bring a claim for additional remuneration or compensation. In order to succeed in such a claim, the contractor will need to meet a high burden of proof.

This approach is mirrored by the VOB/B standard terms and conditions, as well as German law governed FIDIC contracts (which, in recent editions, define force majeure events as “exceptional events”).

However, the concept of frustration is not recognised under German law. If and to the extent that an event of force majeure makes it impossible for a contractor to perform the contract, the respective obligations will be suspended for the period during which the event continues.

It is important to note that German law and standard construction contracts require the contractor to notify the employer immediately upon the occurrence of a force majeure event, otherwise it may not be possible to make a resulting claim.

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Suspension

As noted, force majeure itself does not relieve a contractor from their obligations under a construction contract, unless explicitly provided for in the contract (as is usually the case in FIDIC contracts). Where no such provision is in place, the statutory legal concept of impossibility applies, meaning a party will be relieved from liability to perform to the extent, and for the period during which, performance of its obligations is not possible.

Accordingly, in the case of a force majeure event such as COVID-19, where a party is unable to perform its contractual obligations, the relevant obligation will be suspended until the event has passed. The affected party must notify the counterparty immediately and, as far as possible, limit the consequences of such an event.

Depending on the circumstances, the owner may still be obliged to make payment in relation to works already performed. However, any additional costs resulting from the suspension of the contract will be borne by the contractor unless the parties have explicitly agreed otherwise.

Some bespoke contracts, as well as FIDIC contracts, include more detailed clauses concerning contract suspension, and respective notification obligations.

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Termination

German construction contracts that follow the VOB/B's standard terms and conditions provide that both parties may terminate if a force majeure event continues for more than 90 days. However, this time period is often extended in contracts concerning large-scale construction projects, particularly those subject to debt financing.

Under the German Civil Code, any party wishing to terminate a construction contract must demonstrate that completion will cause 'unbearable hardship', taking into consideration principles of good faith and the interests of the counterparty. As is the case in relation to suspension, they will not usually be entitled to claim for additional costs or compensation, save in exceptional circumstances of "unbearable hardship".

Further, several restrictions under German insolvency law may prevent the unilateral termination of a contract in the event of a party's insolvency.

Practical advice

Parties to German construction contracts should review any applicable force majeure provisions in the context of the applicable statutory principles, seeking legal advice as appropriate and certainly before taking any enforcement steps.

In the current circumstances, it is imperative that both parties to a contract closely monitor the specific effects of the pandemic on the performance of their contractual obligations, keeping appropriate records.

In addition, parties should keep up to date with any guidance issued on the handling of construction contracts affected by the pandemic. At the time of writing, the German public authorities have published initial guidelines on the evidence required from contractors to successfully claim an event of force majeure under construction contracts with public authorities. Further guidelines are expected to be issued soon.

Should a contractor wish to conclude a new construction contract, this must include clear contractual provisions dealing with the risk of additional costs and time delays or it may be difficult to claim any subsequent compensation.

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KEY CONTACTS



DR CHRISTIAN BAUER
PARTNER • MUNICH

T: +49 89 237 086 123

cbauer@wfw.com



PHILIPP KÄRCHER
PARTNER • FRANKFURT

T: +49 69 297291 215

pkaercher@wfw.com

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